



## IFRS FOUNDATION CONSULTATION PAPER ON SUSTAINABILITY REPORTING

Issued 21 December 2020

ICAEW welcomes the opportunity to comment on the IFRS Foundation's Consultation Paper on Sustainability Reporting, published in September 2020, a copy of which is available from this [link](#).

ICAEW welcomes this important consultation from the IFRS Foundation. There is a pressing need for the development of a global set of high quality, authoritative sustainability reporting standards and we believe the IFRS Foundation is in a strong position to help achieve this goal. We urge the Foundation not to delay in taking the next steps to set up a Sustainability Standards Board and to set it to the task of developing sustainability reporting standards.

This response of 21 December 2020 has been prepared by the ICAEW Financial Reporting Faculty. Recognised internationally as a leading authority on financial reporting, the faculty, through its Financial Reporting Committee, is responsible for formulating ICAEW policy on financial reporting issues and makes submissions to standard setters and other external bodies on behalf of ICAEW. The faculty provides an extensive range of services to its members including providing practical assistance with common financial reporting problems.

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## KEY POINTS

### Support for global sustainability reporting standards

1. ICAEW welcomes this important consultation from the IFRS Foundation. There is a pressing need for the development of a global set of high quality, authoritative sustainability reporting standards and we believe the IFRS Foundation is in a strong position to help achieve this goal. As such, we support the Foundation's proposal to expand its remit and to establish a Sustainability Standards Board (SSB) to set sustainability reporting standards.
2. We consider the Foundation's well-established and robust governance structure to be fundamental to the development of high quality and proportionate sustainability standards. We also count as key strengths of the proposal the Foundation's experience in developing rigorous and transparent due process, its existing relationships with a broad range of external stakeholders, and the natural linkage with financial reporting.
3. We urge the Foundation not to delay in taking the next steps in setting up the SSB and setting it to the task of developing standards. As discussed below, there is considerable support and momentum behind the development of a truly international corporate reporting system and, in our view, now is the time to act.

### Building on existing initiatives

4. It will be essential for the Foundation to build on and work with existing frameworks, standard-setters and regional initiatives, which may have the force of law. It must also galvanise these various organisations and build on the current momentum and willingness to collaborate. We believe the Foundation has much to offer to this process, but without the support, experience and expertise of existing initiatives and standard-setters, the chances of success will be severely diminished.
5. We also note that this is a rapidly evolving area, with significant developments occurring on a regular basis. In particular, we point to the recent announcement that the IIRC and SASB intend to merge to form the Value Reporting Foundation. This is an important development and, in many ways could be viewed as a natural and important starting point for the Foundation's planned SSB.
6. Another important development is the European Commission's mandate to EFRAG to undertake preparatory work for the elaboration of possible EU non-financial reporting standards. In our view, the work of EFRAG could helpfully contribute to the Foundation's proposal to develop sustainability reporting standards. We call on both the Foundation and EFRAG to adopt an outward looking, streamlined and collaborative approach, committed to the ultimate end goal of developing global reporting standards for sustainability.

### Scope and priorities

7. We agree that, as a priority, the SSB should start by developing a sustainability reporting standard on climate-related disclosures. However, we urge the SSB not to produce this standard in isolation, particularly as climate is related to many other sustainability topics such as water, biodiversity and inclusion.
8. We strongly recommend that the SSB should set out a 5-year plan, explaining what standards it expects to produce on a broader range of sustainability matters. This plan should outline the matters to be covered, in what order, and the proposed timetable. We also suggest that the SSB outlines which projects are priority areas and which topics require further research. Taking this approach would provide clarity of direction while allowing more pressing areas to move ahead without delay.

### Materiality and intended audience

9. Through our discussions, we are aware of some confusion over how the concepts of 'financial materiality' and 'double materiality' have been described in the consultation paper. For the avoidance of doubt, our understanding of 'financial materiality' is that it would require

the provision of information about the impact of relevant events on the reporting entity **and** information about the impact of the reporting entity on the wider environment and stakeholders. In both instances, this information would be required to the extent that – if omitted – it could influence the decisions of investors or other users of the financial statements who are interested in the performance and long-term financial health of the reporting entity.

10. It is on the basis of this understanding that we agree that the Foundation should initially follow a ‘financial materiality’ approach and focus on providing sustainability information most relevant to investors and other market participants. This is more likely to attract support from global capital markets as it meets the needs of investors, as discussed in paragraph 49 of the discussion paper. In the next stage of this project, we suggest that the Foundation should clarify how ‘financial materiality’ would apply to non-financial information and explain what type of non-financial information would be captured.

### Maximizing success

11. This is a critical juncture in the journey towards the development of global standards for sustainability reporting and the Foundation’s proposals are an important step in the right direction. We highlight below some key matters that in our experience will need to be considered closely in the coming months:
- The establishment of the SSB is conditional upon certain requirements for success being met. Flexibility and judgement will be important to ensure there is not any undue delay in getting this project started [see question 3].
  - The SSB will need to consider what the broader requirements for success should be for the sustainability reporting standards themselves, including for example, reaching a consensus on the purpose and objective of the standards [see questions 3].
  - The Foundation will need to consider, at an early stage, how the standards might be adopted at a jurisdictional level. The Foundation will need to build on its existing relationships with jurisdictional regulators and standard setters and endeavour to understand what these stakeholders are seeking from sustainability reporting standards, as this will help frame the task ahead [see question 4].

These matters need proper consideration in order that the SSB’s work and the resulting standards are framed in the right way and address the needs of stakeholders. This could affect the extent to which the standards are adopted around the globe.

12. We also recommend consideration is given to the name of the proposed board and standards. We are concerned that reference to ‘sustainability’ might suggest that only the standards produced by the SSB address sustainability matters ie, that sustainability matters are not relevant to financial reporting standards. In our view, using the term ‘non-financial information’ would be a more accurate description, would avoid confusion over how sustainability matters are addressed more broadly in corporate reports, and potentially would provide more flexibility in the scope of topics that might be addressed by the standards.

## ANSWERS TO SPECIFIC QUESTIONS

### Question 1

***Is there a need for a global set of internationally recognised sustainability reporting standards?***

***(a) If yes, should the IFRS Foundation play a role in setting these standards and expand its standard-setting activities into this area?***

***(b) If not, what approach should be adopted?***

13. Yes, we believe there is a pressing need for the development of a global set of high quality, authoritative sustainability reporting standards. Issues such as climate change, environmental degradation, human rights and other social issues are a growing concern to a

wide range of stakeholders. Yet at the same time, the non-financial reporting landscape appears more fragmented than ever, with new requirements, initiatives and guidelines continuing to emerge on a regular basis.

14. In ICAEW's position paper *Non-financial reporting: ensuring a sustainable global recovery*, issued in June 2020, we strongly encouraged efforts towards establishing an international and independent non-financial reporting standard-setting body overseen by an authoritative, internationally recognised umbrella body. This could represent relevant public organisations, coordinate activities globally and help cement a common viewpoint on the desired direction of travel.
15. Our position paper also pointed to the global corporate reporting structure put forward in the Accountancy Europe (AE) Cogito paper, *Interconnected standard setting for corporate reporting*, published in December 2019, as a possible model to follow in order to achieve this goal. This model envisaged the restructuring of the Foundation into a body with a broader corporate reporting mandate and the establishment of a new board responsible for setting non-financial reporting standards. We continue to believe that the Foundation has a central role to play in setting sustainability standards and we strongly support developments to expand its standard-setting activities into this area.
16. Importantly, the Foundation has a well-established and robust governance structure. In our view this is fundamental to the development of high quality and proportionate standards, developed in the public interest and underpinned by robust reasoning, careful research and broad consultation. Similarly, the Foundation has experience in developing rigorous and transparent due process which ensures the right balance between technical coherence, consensus building and agility. Drawing on this experience will be important to ensure the long-term credibility and independence of the standard-setting process for sustainability reporting standards.
17. That said, the Foundation must not take it for granted that the existing governance structure and its due process will be a ready-made fit for the purpose of developing sustainability reporting standards. The Foundation has successfully developed its governance structure and due process for developing financial reporting standards over many years, taking into account the needs of those using its standards. It should use this experience and ability to be flexible when developing the governance structure and due process for sustainability reporting standards. For example, it will need to expand outreach to a wider group of stakeholders and ensure appropriate expertise. Similarly, it will be important to have a due process which allows standards to be developed in a timely and responsive way, to evolve over time, and adapt to changes in the external environment and to new sustainability challenges as they arise.
18. Establishing an SSB alongside the IASB also has the crucial advantage of providing a natural link between sustainability reporting standards and financial reporting standards, providing a coherent whole. This linkage is of fundamental importance. A common criticism of the current corporate reporting landscape, in the broadest sense, is the seeming disconnect between ESG reporting, annual reports and the financial statements, including in terms of the underpinning institutional architecture. The Foundation's proposals could help to address this concern.
19. We believe that now is the right time for the Foundation to take this important step. The demand for the Foundation to expand its role into sustainability reporting has increased significantly in recent years. This was demonstrated by the June 2020 *Statement of Intent to Work Together Towards Comprehensive Corporate Reporting* issued by CDP, CDSB, GRI, IIRC and SASB. In this paper, the five framework and standard-setting institutions outlined their commitment to working towards a comprehensive corporate reporting system, and to engage with all stakeholders, including the Foundation, to achieve a globally accepted comprehensive corporate reporting system.
20. We also note the announcement in November 2020 that the IIRC and SASB intend to merge to form the Value Reporting Foundation. We are also aware of other organisations expressing an interest to join forces with this newly unified organisation in the future. In many

ways, this recent development could be viewed as a natural and important starting point for the Foundation's planned SSB.

21. We believe it is essential for the Foundation to work with existing frameworks, standard-setters and regional initiatives. Indeed, it must galvanise these various organisations and build on the current momentum and willingness to collaborate. The Foundation has much to offer in this process, but without the support, experience and expertise of existing initiatives and standard-setters, the chances of success will be severely diminished.
22. Notwithstanding the need to move ahead without undue delay, we recognise the need to balance speed with the need for proper due process and high-quality standards. Ensuring the development of high-quality standards, which are highly regarded, will be vital to ensure the adoption of SSB's sustainability reporting standards around the world, particularly when other frameworks and initiatives are already in place, and in some cases widely used.
23. A balance must also be struck between meeting demand for greater consistency in sustainability reporting and ensuring the overall quality of those standards. We believe that this can be achieved by the Foundation drawing on its extensive experience in governance and due process, while also working together with existing sustainability reporting initiatives.

### **Question 2**

***Is the development of a sustainability standards board (SSB) to operate under the governance structure of the IFRS Foundation an appropriate approach to achieving further consistency and global comparability in sustainability reporting?***

24. In our view, one of the prerequisites for ensuring consistency and global comparability in sustainability reporting (as referred to in the question) is to create a structure and due process which has the ability to produce high-quality sustainable reporting standards. For the reasons discussed above, we agree that developing a SSB under the governance structure of the Foundation (amended as appropriate for the purpose of producing sustainability reporting standards) would contribute to this outcome.
25. It is also important to bear in mind that producing high quality standards alone will not necessarily be sufficient by itself to ensure their widespread adoption. This will require those designing the standards to have a close appreciation of developments elsewhere, the needs of those who might adopt them, and consideration at an early stage of possible impediments to widespread use.

### **Question 3**

***Do you have any comment or suggested additions on the requirements for success as listed in paragraph 31 (including on the requirements for achieving a sufficient level of funding and achieving the appropriate level of technical expertise)?***

26. A certain degree of flexibility and judgement will be required when determining whether the requirements for success have been met sufficiently. It may be that some requirements take longer to develop and evolve over time, whereas others might be achieved more readily. Ensuring a commitment to these success factors with a clear plan on how they will be achieved is important, but it will need to be balanced against the need to move ahead and not lose momentum at this critical juncture.
27. One requirement for success that is not explicitly mentioned is ensuring good quality and robust due process procedures. It may be that the Foundation envisages this to be part of the requirement for 'ensuring the adequacy of the governance structure.' However, in our view the importance of establishing good quality and appropriate due process it is such that it warrants inclusion of a separate requirement for success which can be monitored and measured independently.
28. Stable funding, adequate resources and appropriately skilled and experienced staff are prerequisites for an effectively functioning standard-setter. We agree, therefore, that it will be critical to achieve the level of separate funding required in order to successfully establish the



SSB. It will also be important for the Foundation to ensure funding arrangements which do not result in any real or perceived threat to the independence of the SSB.

29. The current mission of the Foundation is 'to deliver robust, reliable and transparent information as input for the decisions of the primary users of general-purpose financial statements.' While we agree that this mission (which currently relates to financial reporting) should not be compromised, we suggest that the Foundation will need to clarify its mission with regards to sustainability reporting, including reference to the intended primary users of sustainability information. Understanding the Foundation's mission will influence both the development of the SSB and the sustainability reporting standards.
30. We also note that, in due course, it will be necessary for the Foundation to set wider requirements for success for the development of sustainability reporting standards. For example, this might cover matters such as achieving consensus on the purpose and objectives of sustainability reporting standards (individually and as a whole) and what outcomes are expected. We suggest that once the Foundation concludes this stage of the consultation process and has agreed to progress with establishing the SSB, it should publish a further consultation paper setting out these matters at a more granular level.

#### **Question 4**

***Could the IFRS Foundation use its relationships with stakeholders to aid the adoption and consistent application of SSB standards globally? If so, under what conditions?***

31. We agree that for sustainability reporting standards to be successful, the Foundation needs to consider, at an early stage, how they might be adopted at a jurisdictional level. We encourage the Foundation to build on its existing relationships with jurisdictional regulators and standard setters and endeavour to understand what they are seeking from sustainability reporting standards. This will be important to ensure that there is sufficient support for the SSB's plans and increase the chances of the resulting standards being adopted. Engaging in this way will also minimise the risk of major objections being raised at a later stage, or for unhelpful overlaps to emerge in the meantime.

#### **Question 5**

***How could the IFRS Foundation best build upon and work with the existing initiatives in sustainability reporting to achieve further global consistency?***

#### **Question 6**

***How could the IFRS Foundation best build upon and work with the existing jurisdictional initiatives to find a global solution for consistent sustainability reporting?***

32. Our comments below relate to questions 5 and 6.
33. We agree that the Foundation should build upon and work with existing initiatives when it comes to developing sustainability reporting standards. There are significant advantages of taking this approach. In particular:
  - a) It avoids duplication of effort and allows the Foundation to draw on the wide-ranging expertise and experience of existing initiatives.
  - b) It reduces the risk that the sustainability reporting standards will be incompatible with jurisdictional initiatives developing at the same time as the SSB's work.
  - c) It may address concerns that have been raised over the length of time it might take for the SSB to develop sustainability reporting standards.
34. We consider below how the Foundation might build on existing initiatives which specifically relate to the interconnection of financial and non-financial information, with other existing sustainability initiatives, and with jurisdictional initiatives.

### Interconnection of financial and non-financial information

35. To achieve the necessary interconnection between financial and non-financial information, we believe the SSB will need to develop both a conceptual framework for sustainability reporting (see question 7) and an overarching framework for interconnected reporting. The need for an interconnected conceptual framework was also highlighted in the AE Cogito Paper. It stated how the interconnected conceptual framework would need to capture concepts such as: materiality, connectivity, a multi-capital approach, integrated thinking and authenticity, impacts, dependencies and their circularity. It pointed to the work of the IIRC's Integrated Reporting Framework (<IR> Framework) as a useful starting point on this front.
36. We agree that the <IR> Framework is appropriate as it sets out principles and concepts that focus on bringing greater cohesion and efficiency to the reporting process. Under the framework, an integrated report should communicate how an organisation's strategy, governance, performance and prospects, in the context of its external environment, leads to the creation of value over the short, medium and long term. The IASB's Practice Statement *Management Commentary*, which provides a non-binding framework for the presentation of integrated information on financial and non-financial matters, should also be considered. In our view, the <IR> Framework and Practice Statement for *Management Commentary* together provide a useful starting point for the SSB in developing a conceptual framework for interconnected reporting.

### Building on existing sustainability initiatives

37. As noted above, there is a willingness among existing initiatives to work towards the goal of a truly international corporate reporting system and to engage with the Foundation to achieve this goal. In particular, progress is being made by the five framework and standard-setting institutions which issued the Statement of Intent to Work Together Towards Comprehensive Corporate Reporting in June 2020. For example, since then this group has published a separate paper demonstrating how certain components of their frameworks and standards, along with the recommendations set out by the TCFD could be used together to provide a starting point for the development of global standards for sustainability-related financial disclosure. For the reasons discussed, we strongly support an approach which would build on this work and involve collaboration with these organisations.
38. Taking this approach will require careful planning. The SSB will need to assess how the various sustainability initiatives fit together, for example by comparing the nature/scope of content, the intended audience, depth of detail required (including industry-specific information) and any emerging best practice in each area. Having made this assessment, the SSB can assess overlaps and gaps, and identify which elements might usefully form part of a cohesive package of sustainability reporting standards. It might be that a small working group could be set up by the SSB to embark on this task, with relevant input from external stakeholders.
39. While we agree that there is a pressing need to start work on an individual sustainability reporting standard on climate-risk (see our response to question 7), we believe that the Foundation should nevertheless start work on this assessment of existing initiatives, and that this work should be subject to outreach and consultation in the form of a discussion paper. Such a discussion paper might also usefully seek views on which topics should be priority areas for the SSB and which areas might require further research (see question 7). A similar discussion paper was issued in 2004 by the IASB in relation to its work on Management Commentary. It may be helpful for the Foundation to refer back to this earlier discussion paper and the associated feedback. Equally, a similar exercise is being carried by the EFRAG Taskforce for non-financial reporting standards and might provide useful input for the Foundation's own assessment.

### Building on jurisdictional initiatives

40. We believe particular attention should be given to the European Commission's mandate for EFRAG to undertake preparatory work for the elaboration of possible EU non-financial

reporting standards and to provide reflections on changes to EFRAG's due process, governance and funding that might be required in case EFRAG were to be entrusted with a standard-setting role. In our response to EFRAG's recent **Ad personam mandate on Non-financial Reporting Standard Setting** questionnaire we called for the potential development of European standards to be framed in an innovative, outward looking, and collaborative way.

41. This call for an outward looking and collaborative approach applies equally to the Foundation. In our view, the work of EFRAG can helpfully contribute to the Foundation's proposal to develop sustainability reporting standards. For example, the SSB could develop a way of working which is open to building on initiatives developed by the other individual jurisdictions, including the EU, in order to develop a set of global sustainability reporting standards.
42. Importantly, we do not believe that the Foundation's proposal to develop a set of global sustainability reporting standards, the work of EFRAG as noted above, and other jurisdictional initiatives, are mutually exclusive developments. Having a global set of standards can provide a helpful common solution that is scalable and ensures global comparability. However, it does not prevent individual jurisdictions from addressing specific policy objectives, as required.
43. It will be important for the Foundation to be engaged closely with developments in Europe. The European Commission has articulated its desire to achieve progress in this area; in its December 2019 European Green Deal it acknowledges that 'as the world's largest single market, the EU can set standards that apply across global value chains'. This has more recently been elaborated by the Institute for European Environmental Policy which 'recognises that standard setting by the EU in line with its environmental and climate ambitions can, through trade, be a driver for raising standards globally' (IEEP, An EU Green Deal for trade policy and the environment, February 2020). Through EU law and its international trade agreements, which increasingly refer to sustainable development matters, the EC has the means to catalyse action. Successful collaboration and consideration of regional developments will therefore be crucial to wide adoption of the SSB's standards.
44. On a more immediate practical level, enhanced coordination between the key standard-setting organisations boards, especially a potential future SSB, could be framed by a mode of working which encourages:
  - Transparency of work, with the possibility for the key bodies to be able to input into the content of standards under development – with cooperation ensured through respective internal rules of procedure.
  - Avoidance of duplication of work, enabling expertise to be focused and used in an efficient manner.
  - A more rapid process of development and maintenance of standards, by seeking to establish early consensus.
  - Shared commitment to ensure the appropriate involvement by both bodies of all relevant interested parties and stakeholders.
45. Specific steps to encourage enhanced technical cooperation could include:
  - Regular exchange of information, including on draft proposals.
  - Mutual representation at technical working level.
  - The possibility of the key bodies deciding jointly who leads on specific projects.
  - Clarity over likely future work programmes, including an overview of the standards which are deemed necessary and for which there may be 'requests' for work by the standard-setting bodies (while still allowing for the possibility of making urgent 'unplanned' requests to address a specific need).
  - Annual assessment of global alignment efforts, with reference to new, agreed standards, as well as an overview of the collaborative working arrangements in practice.
  - Providing for a mechanism to flag issues of concern.



**Question 7*****If the IFRS Foundation were to establish an SSB, should it initially develop climate-related financial disclosures before potentially broadening its remit into other areas of sustainability reporting?***

46. The question refers to the SSB developing climate-related financial disclosures. For the avoidance of doubt, we have understood this to mean a sustainability reporting standard that would cover matters that would not already be considered and disclosed under existing IFRS, for example, information that might be disclosed as a result of an impairment review. Furthermore, although the question refers to 'financial disclosures', we have assumed that a sustainability reporting standard would also include disclosure requirements for non-financial metrics/information relating to climate change. It is within this context that we respond to question 7.
47. Climate change is an urgent global issue and we agree that, as a priority, the SSB should start by developing a sustainability reporting standard on climate-related disclosures. We strongly support developments which improve the information provided by companies on their climate-related risks and opportunities.
48. Notwithstanding this support, we urge the SSB not to produce a standard on climate-related disclosures in isolation, particularly as climate is related to many other sustainability topics such as water, biodiversity and inclusion. While developing a standard on climate change is undoubtedly a critical and pragmatic first step and would help develop a 'model' that could be applied quickly to other areas, it is a specific matter within a much broader range of sustainability issues.
49. As such, we believe that the development of a sustainability reporting standard on climate-related disclosures should be conducted as part of the SSB's wider plan to develop sustainability reporting standards, including an over-arching conceptual framework for sustainability reporting (perhaps drawing on the existing conceptual framework for financial reporting where appropriate). To be clear, we are not suggesting that work commences on all standards immediately, but rather that the SSB should set out a 5-year plan, explaining what standards it expects to produce (including in what order, the matters to be covered, and its proposed timetable).
50. As part of this plan, we suggest that the SSB sets out which projects are priority areas and which topics require further research. Taking this approach would provide clarity of direction while allowing more pressing areas to be moved ahead quickly. We suggest that one of the priority areas should be the development of a conceptual framework for sustainability reporting. It may be that the framework would need to develop over time, but we caution against developing standards in the absence of even a basic set of high-level principles for reporting on sustainability matters.
51. On a final note, we observe that the success of initiatives such as the Taskforce for Climate-related Disclosures (TCFD) has significantly raised the profile of reporting on climate change in recent years. It provides a framework for embedding sustainability issues and a model for climate and sustainability standards (ie, governance, strategy, risk, performance) which should serve as an important starting point for the SSB. The excellent work carried out already is to be commended. We strongly encourage the SSB to draw on the TCFD framework, including any emerging best practice, in order to expedite its own work in this area. However, we must not lose sight of the many other pressing environmental and social matters which also require urgent action but may not have had the same level of attention and/or do not have well-established supporting frameworks.
52. Indeed, when assessing immediate priorities, the SSB should consider which topics/area would benefit the most from standard-setting activity and where the SSB could usefully provide discipline to a confused area of reporting. As noted elsewhere in our response, steps could be taken to get such projects started quickly and due process could be adapted accordingly to ensure sufficient flexibility but without undermining the overall quality of the resulting standards.

### **Question 8**

#### ***Should an SSB have a focused definition of climate-related risks or consider broader environmental factors?***

53. Similar to our comments to question 7, we agree that the immediate focus should be on climate-related risk. However, this should be developed in the context of being part of wider plan to develop standards on a broader range of environmental and social matters.

### **Question 9**

#### ***Do you agree with the proposed approach to materiality in paragraph 50 that could be taken by the SSB?***

54. Paragraph 46 of the consultation paper refers to ‘financial materiality’ as providing information which – if omitted – could influence the decisions of investors or other users of the financial statements who are interested in the performance and long-term health of the reporting entity. Paragraph 47 states that adopting this approach would focus on information about the effects of relevant events (for example, climate change) on the reporting entity, as this would influence the decisions of investors or other users of the financial statements who are interested in the performance and long-term financial health of the reporting entity. Paragraph 49 then goes on to highlight how a company’s impact on the environment is becoming increasingly important to the investor audience because there is a connection between a company’s impact on the environment and the risks and opportunities for the company.
55. When read together, paragraphs 46, 47 and 49 appear to be consistent with our own broad view of how financial materiality can be applied to non-financial information. However, through our discussions, we are aware of some confusion over how these materiality concepts have been described in the consultation paper. We suggest that the Foundation should clarify how ‘financial materiality’ would apply to non-financial information and explain what type of non-financial information would be captured.
56. For the avoidance of doubt, our understanding of ‘financial materiality’ is that it would require the provision of information about the impact of relevant events on the reporting entity **and** information about the impact of the reporting entity on the wider environment and stakeholders. In both instances, this information would be required to the extent that – if omitted – it could influence the decisions of investors or other users of the financial statements who are interested in the performance and long-term financial health of the reporting entity.
57. It is on the basis of this understanding that we agree that the Foundation should initially follow a ‘financial materiality’ approach and focus on providing sustainability information most relevant to investors and other market participants. This is more likely to attract support from global capital markets as it meets the needs of investors, as discussed in paragraph 49 of the discussion paper. Over time, the Foundation could consider how to broaden its scope to consider information of varying relevance to multiple stakeholders.

### **Question 10**

#### ***Should the sustainability information to be disclosed be auditable or subject to external assurance? If not, what different types of assurance would be acceptable for the information disclosed to be reliable and decision-useful?***

58. In recent years, there has been a significant shift in interest from investors in sustainability disclosures. When such disclosures are material, investors are also increasingly interested in the extent to which this information can be relied upon.
59. This trend would indicate that a move towards auditing or externally assuring sustainability disclosures would be welcomed by investors and other users. However, in practice, there are significant challenges, and other related matters, that require careful consideration before

any decisions are taken. These challenges and matters are summarised in the paragraphs below and explored in more detail in ICAEW's 2019 publication, [A buyer's guide to assurance on non-financial information](#), which was produced in collaboration with the World Business Council for Sustainable Development (WBCSD).

60. With this in mind, we believe it is important for the sustainability reporting standards to be developed in an integrated way with auditors and other assurance providers. This will enable early consideration of any potential audit and assurance issues, helping to ensure that in due course the reported information can be subject to assurance.

### Considerations

61. In our view, the current debate about assuring sustainability disclosures does not deal with the basic challenge of how sustainability information is recorded. It will therefore be important to engage with management reporting software companies at an early stage to think about how accounting systems will capture the information. Without resolving this issue, it will not be possible, for example, for an assurance provider to test the fundamental assertion of completeness ie, whether the disclosed information is complete.
62. Another of the major challenges to providing assurance on sustainability information is the strength of an organisation's control systems and governance structures that support the process of producing the information. A common refrain heard in ICAEW's engagement with assurance providers is that they are often unable to accept engagements for assurance of non-financial information when the organisation's control system is not mature enough, as it leaves them unable to rely on the system as part of the engagement.
63. In order for assurance of sustainability information to become more commonplace, it will be necessary to up-skill boards and audit committee chairs, strengthen the control systems and reporting processes. These are not quick fixes and will take a concerted effort to move forward.
64. For many companies, a significant investment in relevant systems and processes may be required before it is possible to get meaningful assurance on sustainability disclosures. In the short term, a requirement for companies to disclose how their sustainability disclosures are compiled, and how they are updated and internally verified, may help these companies bring the subject of sustainability up the board agenda and to build a business case for more resources in this area.
65. While we note that investors increasingly want to have confidence in material sustainability disclosures, we also find that this does not necessarily translate as a need for external audit or assurance. In ICAEW's 2016 report, [Where next with assurance? The Journey: milestone 5](#), on the subject of narrative information, we find that: 'investors want confidence in information, but they are not interested in how that confidence is achieved. Board members, seeking comfort that they have met the needs of investors, are the people who specify when and where assurance should be obtained. In other words, it is the board that translates investors' need for confidence into a demand for assurance.'
66. It will be important to engage with investors in any discussions about assurance to better understand their views on how confidence in sustainability disclosures can be achieved. For example, providing external assurance on the robustness of the processes and controls used to produce the sustainability information, rather than the disclosures themselves, may be more appropriate. Alternatively, efforts to strengthen an organisation's governance arrangements may provide investors with the necessary comfort that the company is well run and, in turn, that the information provided to them is reliable.
67. In the UK, we are expecting a government consultation on audit reform imminently. We expect that this will cover the 2019 Brydon report<sup>1</sup> recommendations and that the proposals requiring audit committees to publish an audit and assurance policy, which is subject to an advisory vote by shareholders will be particularly relevant to any decisions taken about the

<sup>1</sup> The Independent review by Sir Donald Brydon into the quality and effectiveness of audit published its report *Assess, assure and inform: improving audit quality and effectiveness* in December 2019.

assurance of sustainability disclosures. By facilitating the understanding of the different sources of assurance and types of assurance providers, and better engaging investors in the assurance decisions, this policy may mean that mandating audit or external assurance on sustainability disclosures may not be necessary. ICAEW is currently undertaking a major project on this topic, the results of which are due to be published in early 2021. We would be pleased to provide further details of this project should it be of interest.

68. Also relevant is the ongoing work of the IAASB to develop guidance for practitioners to 'enable more consistent and appropriate application of ISAE 3000 (Revised) to extended forms of external reporting (EER) and greater trust in the resulting assurance reports by users of EER.'

**Question 11**

***Stakeholders are welcome to raise any other comment or relevant matters for our consideration.***

69. We have no further comments at this stage.